



## CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

September 7, 2006

### **H.R. 5503** **FHA Multifamily Loan Limit Adjustment Act of 2006**

*As ordered reported by the House Committee on Financial Services on July 26, 2006*

#### **SUMMARY**

Under the National Housing Act, the Federal Housing Administration (FHA) is authorized to insure private loans used to finance certain multifamily homes, subject to loan limitations specified in appropriation acts. H.R. 5503 would increase the current limit on the value of individual loans that FHA can guarantee in certain high-cost areas of the country under 12 of its 20 multifamily loan guarantee programs, such as housing for moderate and displaced families and cooperative projects. (High-cost housing markets are designated by FHA and include such cities as Boston, San Francisco, and Los Angeles.)

CBO estimates that implementing H.R. 5503 would increase offsetting collections (a credit against discretionary spending) by \$15 million in 2007 and \$75 million over the 2007-2011 period, assuming enactment of the annual appropriation acts necessary to implement the FHA programs and the Mortgage-Backed Securities (MBS) program of the Government National Mortgage Association (GNMA). Such savings would stem from increasing the number of developers who could obtain loan insurance under many of FHA's multifamily loan insurance programs. The budgetary savings would occur because the fees paid to FHA and GNMA are generally estimated to exceed the cost of expected defaults, as measured using the procedures specified in the Federal Credit Reform Act of 1990. Enacting the bill would not affect direct spending or revenues.

H.R. 5503 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would impose no costs on state, local, or tribal governments.

## ESTIMATED COST TO THE FEDERAL GOVERNMENT

For this estimate, CBO assumes that the bill will be enacted near the beginning of fiscal year 2007. The estimated budgetary impact of H.R. 5503 is shown in the following table. The budget impact of this legislation falls within budget function 370 (commerce and housing credit).

	By Fiscal Year, in Millions of Dollars					
	2006	2007	2008	2009	2010	2011
<b>SPENDING SUBJECT TO APPROPRIATION</b>						
FHA and GNMA Spending Under Current Law <sup>a</sup>						
Estimated Authorization Level	-304	-270	-270	-270	-270	-270
Estimated Outlays	-304	-270	-270	-270	-270	-270
Proposed Changes						
Subsidy Costs for FHA's Multifamily Programs						
Estimated Authorization Level	0	-13	-13	-13	-13	-13
Estimated Outlays	0	-13	-13	-13	-13	-13
Subsidy Costs for GNMA's Mortgage-Backed Securities Program						
Estimated Authorization Level	0	-2	-2	-2	-2	-2
Estimated Outlays	0	-2	-2	-2	-2	-2
Total Changes						
Estimated Authorization Level	0	-15	-15	-15	-15	-15
Estimated Outlays	0	-15	-15	-15	-15	-15
Total FHA and GNMA Spending Under H.R. 5503						
Estimated Authorization Level	-304	-285	-285	-285	-285	-285
Estimated Outlays	-304	-285	-285	-285	-285	-285

NOTE: FHA = Federal Housing Administration; GNMA = Government National Mortgage Association.

- a. The figures for 2006 are CBO's current estimate of budget authority and outlays for FHA's multifamily programs subject to the increased loan limitations under H.R. 5503 and for GNMA's Mortgage-Backed Securities (MBS) program under the enacted appropriation levels for this year. The 2007-2011 levels are CBO's baseline estimates of the amount of offsetting collections generated by those programs.

## **BASIS OF ESTIMATE**

The budgetary impact of this legislation would stem from additional offsetting collections recorded because the higher limits for many of FHA's multifamily programs would generate additional mortgage guarantees by FHA, as well as increased guarantee activity by GNMA. CBO estimates that enacting this bill would increase offsetting collections (that is, reduce outlays) by \$75 million over the next five years, assuming the necessary appropriation actions.

## **Proposed Changes**

The maximum amount of a loan that FHA can guarantee for multifamily housing depends on the base loan levels established by FHA, which vary by type and size of housing within a project. For example, the base loan limit for each unit of a building with two-bedroom apartments without elevators is roughly \$54,000. Currently, in regions designated by FHA as high-cost areas, the base loan limit can be increased by up to 270 percent. Thus, in a high-cost region, the loan limit for each unit in a building with two-bedroom apartments without elevators can be as high as \$146,000 (i.e., 270 percent of the base limit). Under H.R. 5503, FHA could increase the base loan limit by up to 315 percent in high-cost areas. (In this example, the loan limit for that two-bedroom apartment could be as high as \$170,000.)

## **Effects on FHA's Subsidy Costs**

The Federal Credit Reform Act of 1990 requires an appropriation of the subsidy costs and administrative costs associated with loan guarantees and direct loan programs. The subsidy cost is the estimated long-term cost to the government of a direct loan or loan guarantee, calculated on a net-present-value basis, excluding administrative costs. Under current law, FHA's guarantees of multifamily loans result in net offsetting collections (that is, negative outlays) on the federal budget because the Administration estimates that guarantee fees collected on those mortgages will more than offset the costs of expected defaults, calculated on a present-value basis. For 2007, CBO estimates that the weighted average subsidy estimate for the multifamily programs subject to the loan limit increases under this legislation is -1.34 percent. In addition, CBO estimates that, under current law, FHA will insure a total of \$7 billion in multifamily loans in 2007.

If FHA made more loan guarantees as a result of the higher cap on the value of loans in high-cost areas, the agency would record additional offsetting collections (which would be a reduction in discretionary spending). According to industry experts, the current loan limits constrain new construction and rehabilitation of multifamily housing. Based on informal surveys of FHA field offices and realtors in certain high-cost areas, CBO expects that, under

H.R. 5503, FHA would insure an additional 35 to 45 loans a year for multifamily projects (with a total face value of about \$1 billion). We expect that the subsidy rate for those loans would be similar to the programs' estimated rate of -1.34 percent for 2007. Thus, CBO estimates that those additional loan guarantees would increase offsetting collections to the FHA (and thus reduce outlays) by about \$13 million annually over the 2007-2011 period.

### **Effects on GNMA's Subsidy Costs**

Changes in FHA's loan limits also would generate savings for GNMA. GNMA is responsible for guaranteeing securities backed by pools of mortgages insured by the federal government. In exchange for a fee charged to lenders or issuers of the securities, GNMA guarantees the timely payments of scheduled principal and interest due on the pooled mortgages that back those securities. Because the value of the fees collected is estimated to exceed the cost of loan defaults in each year (using credit-reform methodology), the GNMA Mortgage-Backed Securities program is estimated to have a subsidy rate of -0.21 percent in 2007, resulting in net receipts on the federal budget.

Because most FHA multifamily loan guarantees are included in GNMA's MBS program, CBO estimates that raising the loan limit would result in additional GNMA collections of about \$2 million a year over the 2007-2011 period. These savings would affect discretionary spending because, like FHA, GNMA requires appropriation action to establish the total amount of its guarantees.

### **INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT**

H.R. 5503 contains no intergovernmental or private-sector mandates as defined in UMRA and would impose no costs on state, local, or tribal governments.

**ESTIMATE PREPARED BY:**

Federal Costs: Susanne S. Mehlman

Impact on State, Local, and Tribal Governments: Sarah Puro

Impact on the Private Sector: Paige Piper/Bach

**ESTIMATE APPROVED BY:**

Robert A. Sunshine

Assistant Director for Budget Analysis